

**ANNUAL REPORT OF THE ACTIVITIES CARRIED OUT BY THE AUDIT COMMITTEE IN 2012**  
**AND PLAN OF ACTIVITIES FOR 2013**

**I – Introduction**

The scope of activities of the Audit Committee of Portugal Telecom, SGPS, S.A. (“PT SGPS” or “the Company”) are defined (a) in its Charter, which comply with all the items defined in legal, statutory and regulatory national rules applicable to this statutory corporate body and also respond to all the responsibilities in the imperative rules applicable to foreign private issuers in the United States of America, as well as (b) with Service Order (*Ordem de Serviço*) 111CA of 23 February 2011, which changed the regulation of the process of approval of significant transactions with related parties.

In accordance with article 423F of the Commercial Companies Code (*Código das Sociedades Comerciais* – “CSC”) the responsibilities of the Audit Committee, as a supervising body of the Company, are as follows: (a) propose to the shareholders’ general meeting the appointment of the Statutory Auditor (*Revisor Oficial de Contas* - “ROC”) and monitor its independence and the statutory audit process; (b) monitor the process of preparing and disclosing financial information; (c) annually prepare a report of its monitoring activities and give an opinion on the Consolidated and Separate Financial Statements and on the Proposals presented by the Board of Directors; (d) monitor the Company’s management and verify the compliance with the law and Articles of Association; and (e) monitor the effectiveness of the risk management, internal control and internal audit systems.

Also, in accordance with the Company’s Articles of Association and the Audit Committee’s Charter, the Committee must supervise the following matters: (a) the qualifications and independence of the External Auditors; (ii) the quality, integrity and effectiveness of the internal control system; (iii) the quality and integrity of the financial information included in the Annual Report; and (iv) compliance by the Company with the applicable legal and regulatory requirements, as well as with the recommendations and guidelines issued by the competent entities. In addition, in accordance with the terms defined in the above mentioned Service Order 111CA, approval of significant transactions with related parties depends upon a favourable opinion of the Audit Committee.

Therefore the Audit Committee presents its annual report on its activities with reference to 2012, as well as its plan of activities for 2013.

## **II – Activities carried out with reference to 2012**

In carrying out its activities and in compliance with its duties and responsibilities, in 2012 the Audit Committee carried out an extensive series of activities, including:

(a) *Appointment and supervision of the qualifications, performance and independence of the Company's External Auditors and Statutory Auditors*

In accordance with the Company's Articles of Association and the Charter of the Audit Committee, the Audit Committee is responsible for appointing and establishing the remuneration of the External Auditor, and to present a proposal to appoint the Statutory Auditor of PT SGPS to the Shareholders' General Meeting, and also to verify the independence of the External Auditor and Statutory Auditor.

In accordance with Recommendation III.1.3 of CMVM's Company Governance Code (2010) (*Código de Governo das Sociedades*) companies must rotate their external auditors at the end of three mandates (when they are for three years), and their possible maintenance beyond that period must be based on a specific opinion of the Audit Committee that expressly considers the conditions of independence of the External Auditor and the advantages and costs of its substitution.

Therefore, for purposes of CMVM' Recommendation and following the verifications already made by PT SGPS' Audit Committee in the beginning of 2011, in 2012 the Audit Committee reviewed the appointment history, qualifications, specialization, independence and professional relationship and possible advantages and costs of substituting PT SGPS' current External Auditor, which at the end of the 2011 audit completed the three mandates of the government bodies, and concluded that there are valid and sufficient bases to maintain the External Auditor responsible for the external audit of the PT Group's consolidated financial statements. On this basis, the Audit Committee believes that the above mentioned Recommendation III.1.3 of CMVM's Corporate

Governance Code has been complied with, and so the Audit Committee decided to renew the corresponding mandate for the years 2012 to 2014.

Considering the assessment of the qualifications and work performed and independence of the Company's External Auditor, the Audit Committee decided to extend the audit contract of the annual consolidated accounts of the PT Group, entered into with Deloitte & Associados, SROC, SA, for the following work for 2012, fixing the corresponding remuneration:

- Simplified audit procedures of the consolidated financial statements of the PT Group as of 31 March and 30 September 2012, involving the identification and analysis of the accounting impact of significant unusual and or non-recurring transactions; and
- Limited review of the consolidated financial statements of PT Group as of 30 June 2012, involving a limited review of the accounts of the most significant subsidiaries in Portugal and of PT International Finance, B.V., as well as accompanying and review the limited review reports of the Oi and Contax Groups and of UNITEL, carried out by other auditors.

As defined in OROC's Articles of Association and the U.S. SEC regulations, direct confirmation was obtained from the External Auditor of their compliance with the applicable independence criteria and the Audit Committee has also made inquiries as to the auditors independence, whenever considered necessary.

In accordance with the Articles of Association and the Audit Committee's Charter, the Audit Committee is fully responsible for the pre-approval of all professional services contracted with the External Auditors, namely of tax consultancy and other services, and periodic monitoring has been made of the work and fees contracted. In this respect, the Audit Committee noted that: (i) the ratio defined for contracting non-audit or audit related services was complied with, which in 2012 represented only 9% of total services contracted;; and (ii) the contracting of such services complied with the rules defined.

In addition, the Audit Committee supervised the compliance with the rules of the U.S. SEC and NYSE, which condition the hiring by the Company of auditor's employees and the rotation of the Partner in Charge of the external audit of the consolidated financial statements of the PT Group.

The Audit Committee also reviewed the independence and the scope, terms and conditions of the services rendered and assessed the quality of the work carried out by the effective Statutory Auditor of PT SGPS, elected by the Shareholders' General Meeting held on 27 April 2012. During the year, the Audit Committee met with the Statutory Auditor on a regular basis and obtained periodic information regarding the work attributed to it.

Considering the results of the above activities, the Audit Committee believes that the Company's External Auditor and the Statutory Auditor acted with independence.

*(b) Supervision of the functions carried out by the External Auditor and Statutory Auditor*

In this regard, the Audit Committee analyzed and approved the work plans of the External Auditor and held periodic meetings with it to assess the work performed and analyze its results, having obtained from the External Auditor: (i) reports on the simplified audit procedures of the PT Group's consolidated financial statements as of 31 March and 30 September 2012; (ii) Limited Review report on the consolidated financial statements for the half year ended 30 June 2012; (iii) Auditors' Report on the consolidated and separate financial statements for the year ended 31 December 2012; and (iv) audit report on the annual consolidated financial statements included in Form 20-F for 2012, as well as on the internal control system relating to financial reporting prepared in accordance with PCAOB standards.

In accordance with the Company's Articles of Association and the Audit Committee's Charter, the Audit Committee is also responsible for supervising the statutory audit procedures carried out by the Statutory Auditor of PT SGPS, which was performed namely by the attendance of meetings with the Statutory Auditor and PT's External Auditor, as well as with the Auditors/External Auditors of the most significant subsidiaries of PT Group, the realization of periodic meetings and discussion of the work plans and the review and discussion of the contents of the statutory audit reports on the consolidated and separate financial statements of PT SGPS for 2012.

Therefore, in 2012 the Audit Committee represented the Company, for all purposes, before the Statutory Auditor and the External Auditor, and reviewed their respective reports; as the Company's monitoring entity, in 2012 the Audit Committee also assessed and monitored performance of the functions of the Statutory Auditor and the External Auditor. In order to assess the performance of the External Auditor, the Audit Committee made specific inquiries of the CEO,

CFO and Corporate Internal Audit and Financial Reporting Directors, so as to obtain their opinion on the quality of professional performance of the External Auditor.

Considering the results of the work carried out, it is the opinion of the Audit Committee that the External Auditor and the Statutory Auditor acted adequately.

(c) Supervision of the quality, integrity and effectiveness of the internal control and risk management systems and of the performance of the functions carried out by the Corporate Internal Audit Department

The quality, integrity and effectiveness of the internal control and risk management systems are, in the opinion of the Audit Committee, the main guarantors of the quality and integrity of the financial information provided by the Company's management, as well as of the observance of the provisions of the applicable laws, regulations and articles of association.

The Company maintains an internal control and risk management system, the Executive Commission being responsible for its implementation, evaluation and compliance. The system complies with all the requirements of the methodology defined by COSO (*Committee of Sponsoring Organizations of the Treadway Commission*) and is subject to systematic assessment and review, being subject to regular audits by both the Corporate Internal Audit Department and the External Auditor; in addition, the PT Group's internal control and risk management system was subject to certification by the External Auditor for 2012 in accordance with Section 404 of SOX. No deficiencies classified as "Material Weaknesses" that could place in doubt either the effectiveness of the PT Group's internal control and risk management system or its adjustment to the needs of the PT Group were reported by the External or Internal Auditor.

In 2012 the Committee continued its work to (i) supervise the quality, integrity and effectiveness of the internal control and risk management system and (ii) monitor the improvements implemented to overcome the insufficiencies. In addition, the Audit Committee periodically discussed and analyzed the application of the system with PT SGPS' Executive Commission and, when considered necessary, with the management of the PT Group main subsidiaries.

In supervising the Internal Audit Function (AIC), the Audit Committee reviewed and approved the Corporate Internal Audit budget, as well as the risks' evaluation and the internal audit plan

proposed for 2013. The Audit Committee had quarterly meetings to accompany the work carried out, in addition to other meetings, as considered necessary, to review the main issues raised and the implementation by the Executive Commission and by other applicable departments of the proposals and recommendations presented in the AIC reports.

*(d) System for reporting irregularities and compliance*

The Company maintains, since 2005, and under the direct functional responsibility of the Audit Committee, a system for the reporting of irregularities, known as Qualified Reporting of Irregular Practices (“whistleblowing”), that ensures confidentiality and anonymity, as required by SOX and other applicable legal provisions. The system covers acts or omissions attributable to the PT Group’s employees that could have an impact on the financial statements or in the information sent to CMVM or the U.S. SEC or that could harm the Group’s assets.

Within the System of Qualified Reporting of Irregular Practices, the Audit Committee has been ensuring the receiving and forwarding of irregularities’ reports. In 2012, the Audit Committee also had quarterly meetings with “Núcleo de Análise de Participações Qualificadas – NAPQ”, responsible, without decision making powers, for the treatment of qualified reports – so that the Audit Committee can analyze and decide on the matters reported, as well as, to introduce improvements to the system and to its internal disclosure.

*(e) Supervision of the quality and integrity of the interim and year-end financial information*

The Audit Committee met periodically with the Executive Director responsible for the preparation and disclosure of financial information, together with those responsible in the Financial Reporting Department, as well as with the Company’s External and Internal Auditors and PT SGPS’ Statutory Auditor, having reviewed the adequacy of the unaudited quarterly information and of the half year and year end information disclosed and its conformity with the applicable legal, regulatory and accounting requirements.

The Audit Committee also met with those responsible in the Financial Reporting Department and separately with the PT's External Auditor, as required by the American auditing standards, namely PCAOB Interim Standard AU 380 - Communication with Audit Committees, inquiring as to:

- (i) The main conclusions of the work relating to the internal control system over the financial reporting process, carried out in accordance with the PCAOB standards, under SOX 2012, including the fact that such work did not identify any deficiency classified as a "Material Weakness", and,
- (ii) the conclusions of the audits of the consolidated financial statements for 2012, 2011 and 2010 to be included in Form 20-F for 2012, to be provided to the U.S. SEC, carried out in accordance with the PCAOB standards, including the fact that such work, did not identify any opinion qualifications.

In this respect, the Audit Committee also reviewed, both the interim and the annual reports of the External Auditor, any references to the accounting principles and valuation criteria used, to the recording of significant, unusual and or non-recurring transactions and to significant judgments made in preparing the financial statements.

In addition to this work relating directly to the preparation and disclosure of financial information, in the area of supervision of the internal control system and compliance therewith, the Audit Committee reviewed the following, together with the PT Group's Corporate Internal Audit Department, External Auditor and Statutory Auditor:

- compliance with the current internal control standards applicable to the closing of the interim and year end accounts and financial reporting and the scope, planning and resources involved in the preparation and disclosure of the financial information; and
- questions or requests for clarification raised with the Company by the regulators of the financial markets, namely the U.S. SEC and the CMVM, as well as the responses presented.

In compliance with the related legal requirements, the Audit Committee (a) participated in the meeting of the Executive Commission in which the annual consolidated and separate financial statements of 2012 were discussed and approved and (b) as required in item 5 of Article 420 of

the Commercial Companies Code, it verified that the report on the structure and corporate governance practices disclosed, included the items applicable to the PT Group referred to in Article 245-A of the Securities Market Code (*Código dos Valores Mobiliários*).

Also, in accordance with the duties of the Audit Committee established in the Company's Articles of Association and in its Charter, the Audit Committee issued its annual report on the Management's Report and the consolidated and the separate financial statements for year 2012, to be submitted by the Board of Directors for approval by the Shareholders' General Meeting.

In carrying out its functions established in its Charter, and considering PT SGPS' position as an issuer of securities on the NYSE, the Audit Committee also: (i) reviewed the section entitled "Operating and Financial Review and Prospects" of Form 20-F for 2012 to be submitted to the U.S. SEC; (ii) reviewed the Company's procedures in the area of the annual certification of the CEO and CFO relating to Form 20-F, in the context of general supervision of the Company's internal control system carried out in 2012; and (iii) issued its opinion to the Company's Board of Directors recommending the approval of the inclusion of the annual audited consolidated financial statements in Form 20-F.

It should be noted that the supervision of the adequacy of the policies, procedures and accounting practices and valuation criteria adopted and compliance with them, as well as of the regularity and quality of the Company's accounting and financial information was carried out essentially through review and discussion of the audit reports issued by the PT SGPS' External Auditor, Statutory Auditor and Corporate Internal Auditors.

(f) Other activities

In 2012, the Audit Committee issued 7 Prior Opinions on Proposals for Related Party Transactions, in accordance with the terms defined in Service Order 111CA of 23 February 2011, as referred to below.

In addition to other interim work described in the Quarterly Reports presented to the Board of Directors, the Audit Committee met formally 14 times in 2012, having as a rule monthly meetings, having prepared minutes of the meetings with descriptions of the main activities carried out and respective conclusions and/or decisions, which were all made unanimously.

At the conclusion of the activities carried out in 2012, the Audit Committee prepared a “Self-Assessment Guide” for this year which was provided to the Board of Directors.

### III – Opinions Issued

With reference to 2012, the Audit Committee issued the following Opinions:

<u>Date</u>	<u>Purpose of the Audit Committee’s Opinion</u>
04/01/2012	Favourable opinion on the contracting of REALLIFE to construct and supply a data centre in Palácio do Gelo, Viseu
27/04/2012	Favourable opinion on the contracting of HEIDRICK & STRUGGLES to carry out the 2012 talent management project
14/06/2012	Favourable opinion on the accompaniment by PT PRESTAÇÕES of the capital increase in BES, through exercise of all the rights of preference in the public share subscription with financial settlement on 11/05/2012
25/10/2012	Favourable opinion on the contracting of IBT – INTERNET BUSINESS TECHNOLOGIES, S.A. to implement the “Realtime” technology in the PT Group’s sites
29/11/2012	Favourable opinion on the contracting of HEIDRICK & STRUGGLES to carry out the climate inquiry project for 2012, except as regards the payment of a success fee, which the Committee believed was not justifiable
29/11/2012	Favourable opinion on the contracting of HEIDRICK & STRUGGLES to carry out a consultancy project on the contracting, remuneration and evaluation of the PT Group’s executives
18/12/2012	Favourable opinion on proceeding with the negotiations to realize a business concentration between Sport TV+PP TV and Sportinveste Multimédia
26/02/2013	Guide for the Self-Assessment of the Scope and Activities of the Audit Committee for 2012
27/02/2013	Disclosure of the Press Release and Consolidated Financial Statements for 2012
15/03/2013	Reports and opinions of the Audit Committee on the Managements’ Report and Consolidated and Separate financial statements of 2012
17/04/2013	Opinion on the approval of the Inclusion of the Annual Consolidated financial statements of PT SGPS in Form 20-F for 2012, to be submitted to the U.S. SEC

## **IV – Conclusions**

Considering the activities carried out and opinions issued, as explained above, the Audit Committee believes that throughout 2012 it carried out the necessary activities to comply with its competencies, duties and responsibilities, having the means necessary for that purpose, not having found any constraints or limitations to its work.

## **V – Plan of activities for 2013**

For 2013, the Audit Committee intends to continue to fully and effectively comply with its objectives, as well as with the scope of work and the legal, statutory and regulatory requirements applicable to this statutory corporate body, both national and those relating to foreign private issuers in the United States of America, carrying out a plan of activities similar to that realized in 2012.

Lisbon, 17 April 2013

THE CHAIRMAN OF THE AUDIT COMMITTEE

(João Manuel de Mello Franco)

THE MEMBERS

(José Guilherme Xavier de Basto)

(Mário João de Matos Gomes)

CC: STATUTORY AUDITOR PEDRO MATOS SILVA